

REDUCING YOUR LIABILITY FROM A CONTAMINATION/RECALL



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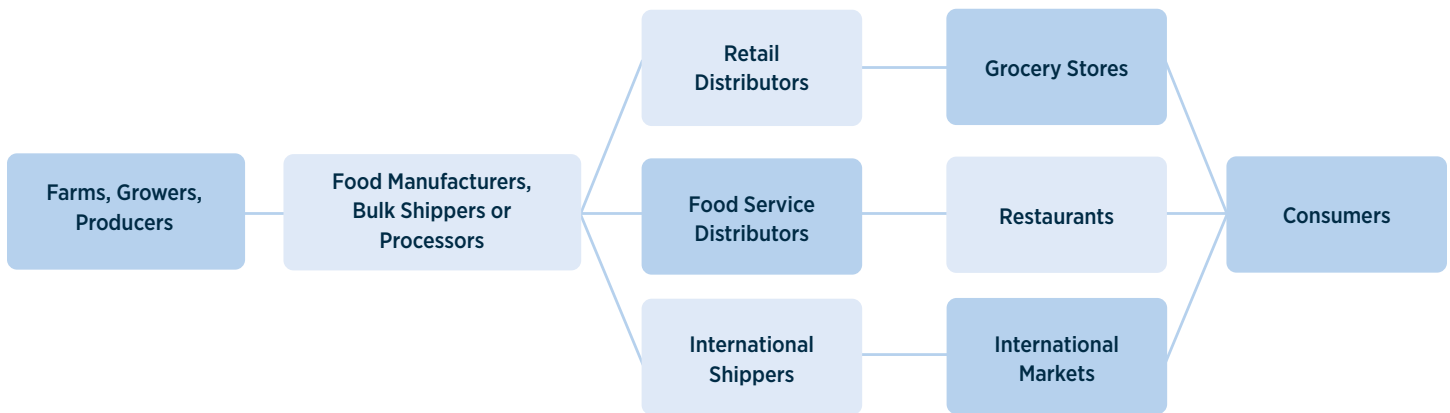
Reducing Your Liability From a Contamination/Recall

The risk of food contamination runs through the entire food supply chain, from farm to fork. While the U.S. food supply chain is well regulated, regulations can't completely eliminate the risk of contamination from foreign materials, chemicals such as cleaning products, pathogens that cause food-borne illness, and allergens that aren't in the ingredient list, such as milk and nuts.

When detected, contamination can trigger a food recall; in 2021, the Food and Drug Administration (FDA) issued 414 recalls of food and beverages.¹ Expert brokers and underwriters anticipate that with increased regulatory attention (now that the pandemic appears to be winding down), stronger science and technology, and traceability, that number will continue to increase.

WHERE CONTAMINATION OCCURS IN THE FOOD SUPPLY CHAIN

The food supply system has many steps, and getting product through every step cleanly and safely is an ongoing challenge. The more steps in the process, the greater the chance of contamination. Here's a look at places in the food supply chain where contamination can occur (not all products go through all steps):



A product's path through the food supply chain isn't always linear, which complicates traceability, logistics, recall efforts and ultimately, determining where liability lies. For example, ingredient suppliers or contract manufacturers might make one product that is ultimately sold under several different retailers' store brands. And some retailers leverage their brands across thousands of different outlets. In both examples, a loss can affect multiple locations and in severe cases, multiple brands and product lines they sell.

When food is recalled or withdrawn, these questions come into play:

- Where did the contamination happen?
- What brands and/or products are affected?
- What is the financial loss — including recall/replacement costs and business interruption of affected parties — and who bears the loss? (Unfortunately, because of the way the food chain works, grocery and restaurant chains take on much of the risk.)
- Did a downturn in sales occur for the contaminated product or similar products?
- How do contracts assign liability and how do insurance policies apply?

¹"STATE OF THE NATION 2022 | Product Recall Data, Trends and Predictions for US Industries," Sedgwick, Brand Protection

HOW CAN INSURANCE PROTECT YOU FROM A FOOD SAFETY INCIDENT?

It's a common misconception that General Liability and Property insurance cover more than they do. For example, many companies assume, incorrectly, that their General Liability policy will protect them from the liability for selling contaminated ingredients to a customer which causes the customer's consequential damages such as business interruption.

Your General Liability policy generally covers bodily injury or property damage that results from consuming or using your product. However, each state (and potentially insurer) differs in how case law and case precedent determine what general liability covers and what is excluded.

Property may cover business interruption as well, but solely as arising out of a covered peril (which are much different from Product Contamination).

Here's an overview of the differences between General or Product Liability coverage and Recall and Product Contamination Insurance Products.

	General or product liability	Recall or product contamination
Trigger	Actual bodily injury and/or property damage to a third party	Actual or imminent bodily injury or property damage due to an accidental or malicious contamination
Covered loss	Indemnity/medical payments and defense costs (cost of suffering or damaged property expenses) incurred by a third-party	<ul style="list-style-type: none"> Recall and replacement costs Business interruption Brand rehabilitation Crisis consulting Third-party consequential damages
Major exclusions	<ul style="list-style-type: none"> Recall of products, work or impaired property* 	<ul style="list-style-type: none"> Competitor contamination Government fines and penalties General or product liability coverage

*Damages claimed for any loss, cost or expense incurred by you or others for the loss of use, withdrawal, recall, inspection, repair, replacement, adjustment, removal or disposal of your product, work or impaired property if such product, work or property is withdrawn or recalled from the market or from use by any person or organization because of a known or suspected defect, deficiency, inadequacy or dangerous condition in it.

What fills the large potential gap in coverage are Product Contamination and Recall insurance programs that address the stages of a recall, ranging from, but not limited to:

- Initial testing and analysis
- Crisis consulting (including PR, testing, regulatory guidance and more)
- Logistics, employee OT, disposal costs and additional warehousing space

- Replacement (or refund/repair) costs
- First-party business interruption
- Brand/Sales rehabilitation costs
- Third-party consequential damages
- Forensic accounting support

Different elements of a Product Recall or Contamination policy are more important, based on your specific risk. If you're making a finished product, terms that cover replacing the product are much higher priority. However, if you're manufacturing an ingredient, the focus is more on the third-party consequential damages, which is the financial loss your customers experience because they used your contaminated ingredient. Other items like shelf-life, customer exposure, scope or distribution and diversification of risk (i.e. products or facilities) are important considerations.

A Product Recall or Contamination policy includes business interruption. Business interruption costs — for you or your customers — can include the following:

- Loss of gross profit from downtime in the plant and inability to produce product
- Suspension of registration of the facility while you clean it and get the FDA's or USFDA's approval to restart
- Decreased demand
- Loss of a corporate contract — there are many examples of companies publicly firing their suppliers or contract manufacturers following a contamination related loss

Finally, it's important that you and your broker carefully review your policy terms and conditions, which may differ from what was requested in your submission. A wholesaler nor the carrier are responsible for ensuring that the quoted coverage, terms and conditions are sufficient to meet your needs or for ensuring that the coverage aligns with your type of business. Only you and your broker are responsible for approving the insurance policy language. Which is why an experienced product recall broker is so important and will ask the right questions and recommend the right coverages (anyone can claim to be an expert, however very few exist).

TRANSFERRING RISK OUTSIDE OF YOUR INSURANCE PROGRAM

In addition to covering product contamination risk with insurance, you can also transfer risk via your contracts by negotiating terms that best position you for an incident — and that position depends on your role in the food supply system (and whether you are a buyer or a seller in a given arrangement).

Terms to focus on include limits of liability clauses, indemnity obligations, reps and warranties, subrogation rights, access to records, insurance requirements, control over the messaging of the recall, etc. Remember to consider jurisdiction-specific rules that might change terms and the impact of the terms across state lines.

REVIEW YOUR PROTOCOLS

To best position yourself for incidents and to mitigate their related losses, pay attention to some of your own internal protocols, such as supplier-approval protocols; consumer-complaint protocols; recall processes or protocols; crisis-response protocols; and any protocols you have in place internally to identify, investigate and respond to an incident.

FIND EXPERTS TO HELP WITH THE RECOVERY PROCESS

Beyond insurance, contracts and protocols, look at the recovery process. Consider what experts you have, internal or external, to guide you through an incident and the loss mitigation or cost recovery process. Be sure you have access to smart, experienced claims advocates who can help you navigate the claim and develop a recovery strategy even before a claim.

Also, working with an experienced forensic accounting firm is important.

Smart, dedicated, experienced advisors can help you get the benefit of what you paid for.

SELF-EVALUATION: RECALL SIMULATIONS

We advise our clients to conduct recall simulation exercises to identify potential issues — not just traceability concerns, but also financial risks. This simulation could include testing protocols and decision-trees, and examining loss limitation or recovery options, including via your contracts and insurance.

Consider how this scenario would play out with your insurance coverage and with the business decisions you might have to make regarding your customers or supply chain. Doing these exercises can help inform your insurance spend and contract negotiations.

Research the risk in your portfolio, including suppliers and scope of distribution:

- What type of companies are involved — big, small, reputable, reliable, collectible, domestic or foreign? Do the companies involved have the financial resources or insurance to cover a large loss that you and potentially your customers incur? (Unfortunately,

many suppliers are far too small to bear financial responsibility for the loss.)

- Are you the only buyer or one of many who might share a contaminated batch?
- Do your suppliers use one source or multiple sources? Do they monitor the financials of their suppliers?
- Do your suppliers require Contamination/Recall liability coverage and audit the policy language?
- Where are your products going — do you know all destinations and implications?
- Based on the findings, determine if you should insure, self-insure or deploy a captive.

HOW CAN GALLAGHER HELP PROTECT YOU FROM THE AFTERMATH OF A RECALL?

It's critical to get the right coverage and terms to make sure your business has the protection it needs, which might be beyond what's covered in your standard policy. Many different Product Contamination carriers are in the market with different forms, so it's important to find the one with forms and wordings that can be customized to fit your operations.

If that customization isn't right, problems can occur where even the best claims process in the world wouldn't help. Working with a broker who understands — and can help you understand — how a Product Contamination policy works alongside your General Liability policy is crucial. So is being confident that your broker has the capability to support you.

Additional Resource:

How Product Contamination Risk Flows Through the Food Supply System On-demand Webinar

Check out our webinar on this topic for insightful guidance about product contamination risks and how they could affect you, your customers and your supply chain.

Key takeaways:

- Gain understanding of your recall-risk and exposure.
- Learn how contracts can help mitigate and/or add to your risk exposure.
- Determine if your insurance portfolio properly addresses this risk.
- Find out the benefits of working with a broker with industry and coverage expertise.
- Obtain knowledge about your supplier's and customer's recall risk and how their risk can become your risk.

View the on-demand webinar [here](#).

About the Authors



Adam Nisenson

Adam Nisenson began his career at the largest wholesale brokerage office in the country (RT Specialty Chicago) where he was a Casualty & Product Recall broker focused on understanding where one policy ends and the other begins. One of his major focuses is designing these policies around these differences and most specifically, what each client does for a living. After helping to grow a book there, he moved over to Marsh to run the Midwest Region for their Product Recall Practice where he co-led their Food & Beverage Center of Excellence before joining Gallagher in 2018.

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Bill Harrison

Bill Harrison started his insurance career with an underwriting position at AIG. He worked his way up from a Regional underwriter to a global position in their Special Services Division which handled several products including Malicious Product Tampering. During this period, Bill rewrote the policy to include Accidental Contamination and other broadening aspects of the coverage to create the coverage we know today. Bill was involved with Underwriting, Marketing and Reinsurance of the division's products. Bill started and led the first Product Recall Practice at Aon in 1999 and did the same at Marsh in 2010, building what was at the time for each, the largest Product Recall books in the world before coming to Gallagher in 2018.

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Steve Kluting

Steve Kluting, Esq., Gallagher's National Director of Product Recall, is an experienced corporate attorney and food industry executive focused exclusively on advising clients in the food and beverage industry, including restaurant and grocery chains. Using his experience as a "food lawyer," certified HACCP manager and industry executive, he acts as a risk consultant to Gallagher's food industry clients and restaurant chain operators, helping them better assess and manage their product contamination and recall exposure; navigate food safety incidents, government enforcement actions and product recalls; evaluate, design, negotiate and place product contamination/product recall insurance; and report to corporate boards regarding company food safety risks. Steve spent more than 13 years as a member of a large, full-service law firm, many as a partner and co-chair of the firm's food industry practice. He focused on serving FDA- and USDA-regulated companies, advising them on the impact of food laws and regulations, crisis preparation and management, M&A and risk management. More recently, he worked as chief strategy officer for a family-owned food wholesaler and retailer. Steve joined Gallagher in 2014 and is 100% dedicated to advising our food industry clients on their food safety risks. He holds a bachelor's degree from the University of Michigan and a law degree from Indiana University.

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